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C O N F I D E N T I A L SECTION 01 OF 04 SHANGHAI 000246

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SUBJECT: S/P DIRECTOR SLAUGHTER DISCUSSES NORTH KOREA, G2, INTERNET, CHINA'S ECONOMY, WORLD EXPO ON VISIT TO SHANGHAI

REF: A) SHANGHAI 229; B) SHANGHAI 231; C) SHANGHAI 232; D) SHANGHAI 233; E) SHANGHAI 241

CLASSIFIED BY: Simon Schuchat, Deputy Principal Officer, U.S. Consulate, Shanghai, U.S. Department of State.

REASON: 1.4 (b), (d)

¶11. (C) Summary: During her visit to Shanghai May 28-31, Director of Policy Planning (S/P) Dr. Anne-Marie Slaughter met with Shanghai academics, the local business community, and Shanghai Expo Bureau officials. The scholars said China is upset by recent North Korean provocations and will likely support further UN sanctions. A regional G-3 institution including the United States, China, and Japan would be preferable to a G-2 and can be expanded to include discussion on security as well as economic issues, said one scholar. Another scholar was favorably inclined towards a G-2 and observed that existing institutions, such as the IMF and the G-8, probably need to be restructured to better meet China's own needs. US business leaders in Shanghai said high-end and low-end consumers in Shanghai have been hit hard by the economic downturn, but the middle class is doing relatively well. They believe EU industry standards are taking root in China and urged more US Government action to promote US industry standards in China. Internet investors see a sharp growth in online gaming in China and discussed the real-life economic impact of China's online virtual currency. Director Slaughter visited the Expo Bureau, where Bureau officials urged the US Government to confirm US participation in the 2010 Shanghai World Expo. End summary.

SASS/Fudan Scholars on Pelosi, North Korea, Pakistan, G-2

¶12. (C) During a lunch meeting with S/P Director Slaughter on May 29, Shanghai Academy of Social Sciences (SASS) Vice President Huang Renwei (one of Shanghai's leading scholars on US-China relations and international affairs) commented that

Speaker of the U.S. House of Representatives Nancy Pelosi's recent visit to China went well, as she discussed "safe topics" with her Chinese interlocutors. Pelosi's reputation as a critic of China's human rights record did not mar the visit, said Huang, since "Chinese leaders do not care" about what was said or done in the past by current leaders. (For more on Pelosi's visit to Shanghai, see refs a-e.)

¶3. (C) Turning to the subject of North Korea, Huang said possible motives for the DPRK's recent nuclear and missile tests include the North's domestic politics and an effort to "make a mess" of domestic politics in South Korea. According to Huang, North Korean officials recently told scholars in Beijing that the North will resume talking once it "feels safe," but Huang believes this is just an excuse. He speculated that the DPRK's recent moves are based on domestic political factors. During the same lunch Fudan University Professor Ren Xiao (an expert on East Asia security and North Korea) said the North's recent provocations signal the growing influence of its military. The DPRK wants to improve its bargaining position vis-`-vis the United States and is looking for a breakthrough in bilateral relations, including a change in America's "hostile policy," which has always been Pyongyang's top priority, said Ren. Huang added that Beijing "feels shame" over recent events since it mediated the Six-Party Talks for years "in vain." China will "take some action," including the probable support of further UN sanctions, and should give a clear warning to the DPRK against further provocations, said Huang. The sanctions, however, should be limited so as to minimize the suffering of ordinary North Koreans. Huang believes the Six-Party Talks will eventually be resumed.

¶4. (C) On Pakistan, Huang Renwei noted that Pakistan has its

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own Taliban, which sometimes works together with the Afghan Taliban depending on the actions of Pakistan's military. China does not fully understand the pro and anti Taliban factions within Pakistan's political and military establishment, said Huang, and China is incapable of influencing all the political parties in Pakistan. He believes there is a good chance of India taking advantage of Pakistan's internal division to launch military action in Kashmir. Pakistan is currently fighting on two fronts, and it is "more afraid" of its eastern front with India. The United States should work with India and China to provide a security guarantee to Pakistan, though Pakistan is currently "suspicious" of all parties, including the United States, India, and China, said Huang. (Note: Huang mentioned that he attended conferences in Islamabad and Karachi followed by a trip to India in April of this year, describing the relatively heavy security measures that the Chinese Embassy in Pakistan used for his delegation. End note.)

¶5. (C) On global governance issues, Huang did not agree with the idea of a G-2 but advocated a regional G-3 (the United States, China, Japan), which, if successful, could eventually be expanded to a regional G-4, G-5, or G-6 (Huang suggested Australia and ASEAN as other potential participants). Such an institution could discuss matters beyond economic issues, unlike APEC which Huang believes is too limited in its focus on economic issues. He added that the United States and China do not exercise enough policy influence in APEC and that even an East Asia Summit which includes the United States would end up as only a talk shop. Fudan University's Ren Xiao thinks it is difficult to coordinate all the 20-plus members of the G-20, though the G-8 appears outdated. How much resource should be put into the G-20 versus the G-8, Ren asked rhetorically. Whether it is the G-20 or G-13, the key is to achieve consensus, particularly between the United States and China, before the actual forum takes place, argued Huang. The consensus can be bilateral or between multiple key players, such as the United States, China, Japan, and the EU, on international monetary and financial reform, Huang added.

¶6. (C) On May 30, S/P Director Slaughter was hosted at lunch by Chen Dongxiao, Vice President of the Shanghai Institutes for International Studies (SIIS). (Note: In 2007-8, Dr. Slaughter spent a sabbatical year from Princeton's Woodrow Wilson School in Shanghai, where SIIS was her administrative base. End note.)

Chen said his current project was to formulate China's "grand strategy" for the new global environment, characterized by a United States that is very powerful but nevertheless no longer paramount. Dr. Slaughter noted that she, too, was engaged in defining a "grand strategy" for the United States, taking into consideration a similar perception of the evolving global environment; the United States now had to exercise "cooperative leadership" because it could only solve problems together with other powers. This led into a discussion of the institutional basis for global governance. Chen was favorably inclined towards a G-2, and observed that existing institutions, such as the IMF and the G-8, probably needed to be restructured to better meet China's own needs. Dr. Slaughter pointed out that it would be difficult to selectively reform international institutions. For example, states whose agreement might be needed in order to reform the IMF may well have their own objectives with respect to reforming the UN Security Council, and for China to achieve the former it would probably be necessary to also accede to the latter in some manner. Dr. Slaughter did not believe that a G-2 would be possible, since there were too many other powers that would see it in their interests to block. She characterized the current global environment as one of "many rising powers" in which problem

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solving would increasingly depend on ad hoc coalitions.

¶7. (C) S/P Staff James Green, accompanying Dr. Slaughter, noted S/P was one of the offices in the State Department currently preparing for the first round of the Strategic and Economic Dialogue (SnED), to take place at the end of July. On both sides, there were issues of coordination that needed to be resolved. In the U.S. system, the Secretary of State, while not directly overseeing other cabinet Departments that might be involved in the SnED, did have statutory responsibility for all foreign relations, whether carried out by the State Department or, for example, the Environmental Protection Agency. However, we were not clear what entity might have the same coordinating function on the Chinese side. Chen responded that the various leading groups at the highest levels, such as the "foreign affairs leading group" or the "Taiwan affairs leading group," were the main coordinating bodies at the center. These groups were made up, at least, of Central Committee members -- more often, Politburo or Standing Committee members, advised by various ministries and think-tanks. Chen further observed that, unfortunately, it was more difficult for the Foreign Minister to exercise supervision over other Ministries and that there was currently some discussion about strengthening the authority of the Foreign Minister in this regard.

U.S. Business Leaders on the Chinese Economy

¶8. (SBU) During a roundtable discussion with S/P Director Slaughter on May 28, U.S. business leaders from the American Chamber of Commerce (AmCham) in Shanghai and The US-China Business Council (USCBC) offered views on the impact of the economic downturn on the local economy. James Rice, Vice President of Tyson Foods' Shanghai office, said his company has not experienced a drop in sales, though customer growth has slowed. Godfrey Firth, Chief Representative in Shanghai of USCBC, said the downturn has "squeezed out inefficiencies" in the manufacturing and export industries in China. Murray King, Managing Director in Shanghai of APCO Worldwide, a consulting firm, said Shanghai has suffered through the downturn, as its GDP grew by 3.1 percent in Q1 2009 compared with 9.2 percent a year ago. High-end luxury services and goods in Shanghai have been hit particularly hard, he added. Firth said that the middle class in Shanghai is still doing "okay" and is starting to buy again, whereas the lower class has suffered considerably but were not major consumers anyway. On Chinese government stimulus measures, Kenneth Jarrett, Vice Chairman of APCO

Worldwide, said government money is flowing into rural healthcare, which could provide a good opportunity for foreign firms with advanced healthcare technology. He said U.S. construction firms like Caterpillar have been "secondary beneficiaries" of China's economic stimulus. However, there has been local protectionism, said King, especially in the auto sector, as local governments have favored the procurement of locally produced vehicles over foreign-made and even over made elsewhere in China vehicles.

¶9. (SBU) On IPR, Manager of Business Advisory Services at USCBC Eric Arndt said the situation differs from province to province.

Chinese SOEs, in some cases encouraged by the government, are engaging in commercial espionage and trying to turn foreign advanced technology into Chinese indigenous technology, said Murray King of APCO. Our interlocutors argued that the United States has fallen behind the EU in setting industry standards in China. The EU funds training programs in China and in Europe for Chinese standards writers and standards implementers, they said. The United States needs to make a more concerted effort to promote its standards in China, or else EU firms will gain a significant advantage over US firms in China, said Tyson's Rice.

Arndt added that hundreds of new industry standards are being

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issued every week in China, and that most follow EU standards. On US participation in the 2010 Shanghai World Expo, Firth said that Coca-Cola and GM are official sponsors, so regardless of whether or not there is a US National Pavilion, the United States will be involved. One interlocutor said it would be a "disaster" if there is no US Pavilion.

Internet Entrepreneurs on China's Online Future

¶10. (SBU) S/P Director Slaughter discussed ways in which the Chinese are connecting online with China-based internet entrepreneurs and investors during a meeting on May 29. William Bao Bean, Partner of Softbank China and India Holdings, a Shanghai-based venture capitalist firm that invests in internet start-ups, talked about italki, a language learning website based in China in which his firm is heavily invested. Bean discussed, for example, how the website links Farsi teachers in Iran with students in New York. He said Tibetan has been a popular language, and the Chinese authorities have not obstructed engagements between Tibetan teachers and students worldwide so far. He added that there were problems in the past with the website being used as a tool of Islamic Jihad, though he did not elaborate on this. Dan Brody, CEO of Koolanoo Group, a Beijing-based venture capitalist firm, said his company runs a social networking site "360Quan" (ranked number 3 in China in user traffic, according to Brody) in which hundreds and thousands of users organize into "clans" to discuss everything from online gaming to favorite actors. The Chinese Government has been closely monitoring the site, said Brody, though most of the activity on the site has been non-political. Brody further discussed the phenomenon of online games and internet cafes, which he called the "opium dens of the 21st century" for an increasing number of Chinese youth. Sage Brennan, a self-described new media expert and former executive at the Hong Kong-based hedge fund Pacific Sun Investment Management, said the virtual currency "QQ" is now hugely popular in China and can be used to buy many things in the real world, including even automobiles in some areas. The Chinese Central Bank has been tracking this "shadow currency" because of its inflationary impact in some local communities, said Brennan.

Visit to Expo Bureau

¶11. (SBU) S/P Director Slaughter visited the Shanghai 2010 Expo Bureau on May 29 and met with Zhou Jun, Director of International Participants Department, and Si Yan, Senior Program Officer of the International Participants Department. Zhou expressed the Bureau's hope that the U.S. Government would confirm participation in this "important event," stressing that more than 190 countries have already confirmed participation and lamenting that only the United States, Andorra, and countries

lacking diplomatic ties with China have not confirmed participation. During a tour of the Expo site, our Expo Bureau hosts showed Director Slaughter the Chinese Pavilion, the work already fully underway on many other national pavilions, the beginning of the raised central Expo walkway, and the planned site for the US Pavilion (complete with several bulldozers at work clearing the site even on a Chinese holiday). Zhou commented that the Expo Bureau had reserved one of the "best" locations in the entire Expo for the US Pavilion (near a main gate, off the main walkway, near a warehouse, etc). Director Slaughter told Zhou that she would convey the Expo Bureau's message to Secretary Clinton.

¶12. (U) S/P Director Slaughter has cleared this report.
SCHUCHAT